

**STATE OF UTAH INSURANCE DEPARTMENT**

**REPORT OF EXAMINATION**

**OF**

**HEALTHWISE**

**OF**

**SALT LAKE CITY, UTAH**

**as of**

**December 31, 2001**



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February 24, 2003

Honorable Merwin Stewart  
Insurance Commissioner  
State of Utah  
State Office Building, Room 3110  
Salt Lake City, Utah 84114

In accordance with your instructions and in compliance with Utah Code Annotated (UCA) Section 31A-2-203, an examination has been conducted as of December 31, 2001, of the financial condition and affairs of

**HEALTHWISE**  
**Salt Lake City, Utah**

a health maintenance organization, hereinafter referred to as the Organization, and the following report of examination is respectfully submitted.

**SCOPE OF EXAMINATION**

**Period Covered by Examination**

The Organization was last examined as of December 31, 1998, by an examiner representing the Insurance Commissioner of the State of Utah. The current examination covered the intervening three year period through December 31, 2001, including any material transactions and/or events occurring subsequent to the examination date and noted during the course of this examination.

**Examination Procedure Employed**

All phases of the examination were conducted to determine compliance with generally accepted regulatory accounting and valuation standards and procedures promulgated by the National Association of Insurance Commissioners (NAIC), applicable laws of the State of Utah and insurance rules promulgated by the State of Utah Insurance Department. A certificate of representation attesting to the Organization's ownership of all assets and to the nonexistence of unrecorded liabilities was obtained from management. Reliance was placed on certain workpapers generated by the certified public accounting (CPA) firm retained by the Organization for its annual statutory audit as of December 31, 2001. Those workpapers included the evaluation of internal controls.

**Status of Adverse Findings, Material Changes in the Financial Statement and Other Significant Regulatory Information Disclosed in the Previous Examination**

Items of concern noted in the previous report of examination have been properly addressed by the Organization during the current period of examination.

## **HISTORY**

### **General**

The Organization was originally formed and commenced operations on April 22, 1981, as a line of business of two non-profit corporations – Blue Cross of Utah and Blue Shield of Utah. These corporations were consolidated on January 1, 1982, into Blue Cross and Blue Shield of Utah.

The Organization was incorporated August 10, 1982, under the laws of the State of Utah as a capital stock, for profit, health maintenance organization. The Organization commenced business as a separate entity on September 1, 1982, and was granted a Federal Certificate of Qualification on August 8, 1984.

Blue Cross and Blue Shield of Utah owned 100% of the outstanding stock of the Organization from January 1, 1982, to December 1986, at which time ownership of all corporations affiliated with Blue Cross and Blue Shield of Utah was transferred to BCSU Corporation. BCSU Corporation filed Articles of Dissolution on December 31, 1987, and ownership of the Organization reverted to Blue Cross and Blue Shield of Utah in January 1988.

In May of 1996, Blue Cross and Blue Shield of Utah announced its intention to affiliate with The Benchmark Group, an Oregon nonprofit corporation consisting of Blue Cross and Blue Shield plans located in the Northwest. On August 1, 1997, The Benchmark Group became known as The Regence Group. Blue Cross and Blue Shield of Utah's name was changed to Regence BlueCross BlueShield of Utah during December 1997.

### **Capital Stock**

The Organization authorized 300,000 shares of stock each having a par value of \$10. The number of shares issued and outstanding as of yearend 2001 were 23,336, which were all owned by Regence BlueCross BlueShield of Utah.

### **Dividends to Shareholders**

No dividends were declared or paid throughout the period of examination.

### **Management**

Management of the property, affairs and business of the Organization was vested in a board of directors, which according to its bylaws would consist of no less than seven (7) nor more than ten (10) members. The following persons had been duly elected to a one-year term by the shareholder on March 22, 2001, and were serving as directors of the Organization:

Name and Residence

Principal Business Affiliations

E. John Ruch  
Lewiston, Idaho

Chairman of the Board and Chief Executive Officer, Healthwise  
Chief Executive Officer, Regence BlueCross BlueShield of Utah  
President and Chief Executive Officer, Regence BlueShield of Idaho

D. Scott Ideson  
Park City, Utah

President, Healthwise  
Senior Vice President, Regence BlueCross BlueShield of Utah

Michael N. Mitchell  
Sandy, Utah

Vice Chairman of the Board, Healthwise  
Senior Vice President, Regence BlueCross BlueShield of Utah

Donald E. Smith  
Salt Lake City, Utah

Senior Vice President, Regence BlueCross BlueShield of Utah

Thomas W. Colosimo  
Lewiston, Idaho

Treasurer, Healthwise  
Vice President and Chief Financial Officer, Regence BlueCross BlueShield of Utah  
Vice President and Chief Financial Officer, Regence BlueShield of Idaho

Jacqueline E. Wells  
Park City, Utah

Secretary, Healthwise  
Senior Vice President, General Counsel and Secretary, The Regence Group

Philip L. Bryson, M. D.  
Salt Lake City, Utah

Vice President and Medical Director, Regence BlueCross BlueShield of Utah

Dan L. Chichester, M. D.  
Salt Lake City, Utah

Physician

Thomas H. Caine, M. D.  
Salt Lake City, Utah

Faculty, University of Utah School of Medicine

Ed P. Mayne  
West Valley City, Utah

President, Utah State AFL-CIO

Ernest G. Mantes  
Tooele, Utah

President, Mantes Chevrolet Company

Officers were elected annually by the board of directors. Those serving as of December 31, 2001, were as follows:

<u>Position</u>	<u>Name</u>
Chairman of the Board and CEO	E. John Ruch
Vice Chairman of the Board	Michael N. Mitchell
President	D. Scott Ideson
Secretary	Jacqueline E. Wells
Treasurer	Thomas W. Colosimo

The Organization had one active committee of the board as of yearend 2001, which was a nominating committee. The committee had only two members assigned by the board, Michael N. Mitchell and D. Scott Ideson, which was not in compliance with UCA Subsection 31A-5-412(1) requiring three or more directors on committees designated by the board.

#### **Conflict of Interest**

The Organization had an established procedure for disclosure to its board of directors of any material interest or affiliation on the part of any of its officers, directors, or responsible employees which was in or was likely to conflict with the official duties of such person. No signed conflict of interest questionnaires were provided for the year 2001 for two of the directors, which was in non-compliance with Article VIII of the bylaws of the Organization requiring conflict of interest disclosures on an annual basis by all members of the board.

#### **Corporate Records**

The minutes of the quarterly meetings of the board of directors and annual shareholder meetings for the period covered by this examination were reviewed for conformity to the requirements of the articles of incorporation and bylaws as to matters covered and authorizations made. Approval of all investment activities was noted in all meetings.

The minutes of the board of directors meetings provided no evidence of the election of an assistant secretary or an assistant treasurer for the years 2000 and 2001, as required in Article V, Section 1, of the bylaws of the Organization.

UCA Subsection 31A-2-204(8) requires the Organization to promptly furnish members of the board of directors copies of the adopted report of examination. The minutes did not evidence the presentation of the prior examination report to the directors.

#### **Acquisitions, Mergers, Disposals, Dissolutions, and Purchases or Sales through Reinsurance**

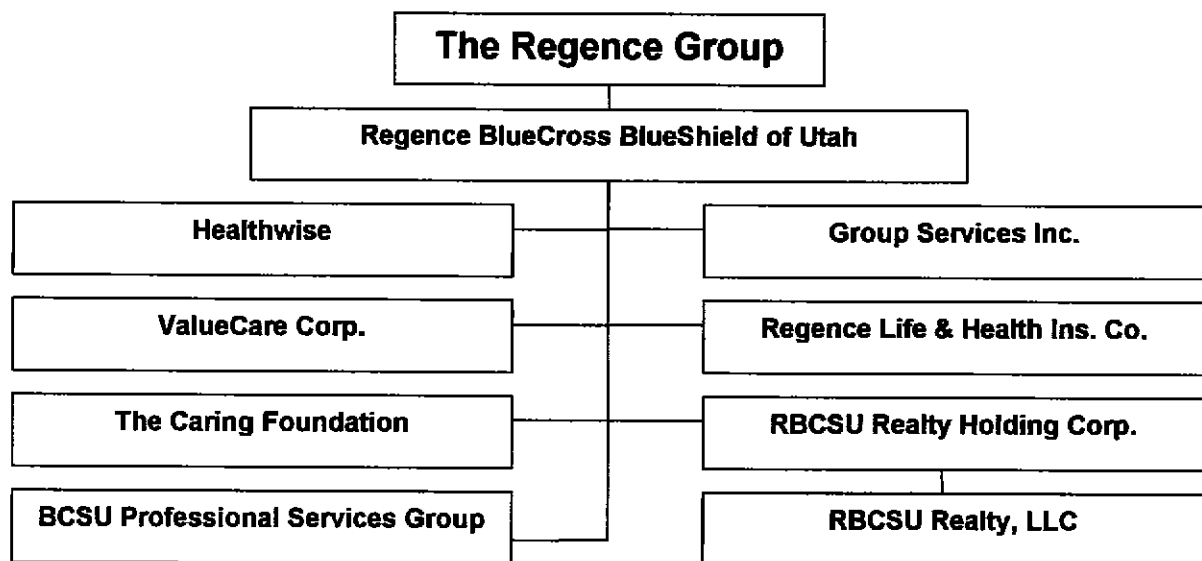
The Organization did not have any acquisitions, mergers, disposals, dissolutions, and purchases or sales through reinsurance.

### **Surplus Debentures**

The Organization did not have any surplus debentures outstanding.

### **AFFILIATED COMPANIES**

Utah Insurance Code Section 31A-1-301(19) defined control as a person who holds, with the power to vote or proxies with the power to vote, 10% or more of the company's voting securities. The Regence Group was the ultimate controlling person under the definition of the Insurance Holding Company Act. The Organization was a wholly owned subsidiary of Regence BlueCross BlueShield of Utah, while The Regence Group was the sole member of Regence BlueCross BlueShield of Utah, a nonprofit corporation. The Regence Group was also the sole member of Regence BlueCross BlueShield of Oregon and Regence BlueShield, a Washington nonprofit corporation, and managed Regence BlueShield of Idaho, Inc., under a management and administrative services agreement approved by the Idaho Insurance Commissioner. The following organization chart illustrates the Organization's immediate affiliate and direct upstream parentage relationships:



The Organization had no ownership interest in affiliated companies.

Affiliate agreements, as itemized below, defined and controlled various aspects of the Organization's transactions and operations.

### **Operating Agreement effective 1/1/88**

Regence BlueCross BlueShield of Utah, the parent of the Organization, agreed to provide services under an operating agreement, including, but not limited to, marketing consultation, advertising and public relations consultation, billing and collection services, certificate accounting, general accounting, investment counseling and electronic data processing. The parent also agreed to provide office space, furniture, equipment, utilities, telephone service, office supplies and other

services necessary for the Organization's continued operations. The parent was reimbursed for actual expenses, allocated in accordance with generally accepted cost accounting principals. The term of the agreement was extended from year to year and may be terminated by either party with a one-year written notice.

#### Financial Agreement

The parent agreed to provide the Organization, pursuant to an inter-company financial agreement, initial and sustaining financial support and accept reinsurance of risk. Reinsurance is discussed below under the section of this report entitled "Reinsurance." The parent also agreed to provide, in the event of the Organization's insolvency, benefits to the Organization's members according to the Organization's certificates after allowing for any contributions from local, state or federal guaranty funds, until the expiration date of the certificates.

#### Advance Agreement

Pursuant to inter-company advance agreements between the Regence BlueCross BlueShield of Utah, Healthwise, ValueCare and Group Services, Inc., advances between the entities became subject to interest. The rate of interest was the prime interest rate as of January first of the calendar year.

#### Service mark and trade name license agreement

The Organization, as a controlled affiliate of The Regence Group, was party to a controlled affiliate license agreement with Blue Cross Blue Shield Association under which it was granted license to use the Blue Shield, the Blue Shield Design, the Blue Cross, the Blue Cross Design as service marks and the terms Blue Shield and Blue Cross in a trade name within certain limitations pursuant to the agreement.

#### Consolidate Tax Agreement

The Organization was party to a consolidated federal income tax filing arrangement effective January 1, 1997. Parties to the agreement included The Regence Group and its subsidiaries as listed on an addendum to the agreement.

### **FIDELITY BOND AND OTHER INSURANCE**

Regence BlueCross BlueShield of Utah, the parent of the Organization, provided fidelity insurance coverage for a limit of up to \$5,000,000 per occurrence with a \$50,000 deductible. The Organization was included as a named insured on the bond. The minimum amount suggested by the NAIC for the Organization was \$400,000. The parent also provided coverage for computer crime, fiduciary liability and directors and officers liability with coverage limits of \$10,000,000 to \$15,000,000 per occurrence or per claim.

### **PENSION, STOCK OWNERSHIP AND INSURANCE PLANS**

All management and administrative duties necessary for the Organization's operation were preformed by officers and employees of The Regence Group, its affiliates, and Regence BlueCross BlueShield of Utah on behalf of the Organization. The Organization had no pension, stock ownership or insurance plans.



## **STATUTORY DEPOSITS**

United States bonds, having an aggregate par value of \$550,000 and a market value of \$570,548, were confirmed to be on deposit with a local depository as of December 31, 2001, and designated as special deposits for the Utah Insurance Department. Securities actually on deposit were not consistent with those on record with the Utah Insurance Department as statutory deposits. Those on record with the Utah Insurance Department included a matured bond that had been sold and was not in the possession of the Organization as of December 31, 2001. Transfer of statutory securities without the approval of the Insurance Commissioner was in noncompliance with UCA Subsection 31A-2-206(10).

The Organization had no statutory deposits other than those designated for the Utah Insurance Department.

## **INSURANCE PRODUCTS AND RELATED PRACTICES**

### **Policy Forms and Underwriting**

The Organization was at risk for group medical services under agreements with its subscribers, and provided medical services to non-insured groups from which it received medical reimbursements and administrative fees. They also were at risk for Medicare supplement benefits under agreements with individuals. They retained all of their group dental and individual Medicare supplement business and \$50,000 of each risk for their group medical business.

### **Territory and Plan of Operation**

The Organization operated solely in the State of Utah and was licensed to conduct business as an HMO class insurer.

New and renewal business for the various lines of business was solicited by outside, independent agents and in-house marketing representatives that worked with the outside agents. All sizes of groups and individual Medicare supplement business were targeted under this marketing system.

The Organization contracted with 2,500 physicians, hospitals, dental and other service providers at the end of the year 2001.

### **Advertising and Sales Materials**

The Organization provided no advertising specifically relating to it.

### **Treatment of Policyholders**

A review of the Utah Insurance Department consumer complaint database report revealed no significant issues or any trends of policyholder mistreatment.

The Organization maintained an appeals log which included comprehensive detail on each complaint, its origin and its disposition. Complaints received from the Utah Insurance Department were maintained on a separate log within the Organization's legal department.

## **REINSURANCE**

The Organization ceded claims for incurred services that exceed \$50,000 per calendar year per member (excluding dental subscriber certificates and Medicare supplement contracts) to its parent, Regence BlueCross BlueShield of Utah, under the financial agreement discussed in the section of this report entitled "Transactions with Affiliates". Provisions included a limit of one year on the run out of paid claims after the calendar year the claim was incurred, after which the parent would not be liable for any further claims. The premium for this coverage was 7.5% of earned subscriber premiums (excluding dental and Medicare supplement premiums).

## **ACCOUNTS AND RECORDS**

The Organization's accounting system consisted of a general ledger, registers, statistical and other records maintained primarily on information systems equipment and software owned by the parent of the Organization under the operating agreement between them. Periodic journal entries were posted to the Organization's general ledger systems, and periodic reconciliations were performed.

A general ledger trial balance was taken as of December 31, 2001, and was reconciled to the Organization's 2001 annual statement. Changes in ledger assets and surplus during 2001 as reported in the annual statement were also confirmed. General ledger accounts for other years covered in the examination period were reconciled to the related annual statement accounts as deemed necessary.

General expenses reported in the annual statement were allocated in proportion to reports received from the parent of expenses paid on behalf of the Organization together with allocations of Organization specific expenses.

The Organization's copy of a bank's signatory card was not consistent with the copy of the signatory card provided by the bank. The bank's copy listed as an authorized signatory an official who no longer had any official duties with the Organization, and did not list two individuals who had signatory authorization by the Organization.

### **Annual Statement**

The Organization did not follow the NAIC Annual Statement Instructions on several occasions including the following:

- The jurat page did not list the chairman of the board and chief executive officer or the treasurer as officers of the Organization;
- No amounts were disclosed for common capital stock or gross paid in and contributed surplus on the Liabilities, Capital and Surplus page. Examination revealed that they were included with unassigned funds;
- Part 2, 2A, 2B and 2C of the Underwriting and Investment Exhibit did not disclose any claims liability or reserves for Medicare Supplement;
- Part 2 and 2A of the Underwriting and Investment Exhibit did not disclose any ceded reinsurance amounts paid or payable for applicable lines of business;

- Schedule S, Part 1, Section 2, Reinsurance Assumed for Accident and Health Insurance, disclosed ceded reinsurance recoveries of \$2,547,960 as negative premiums.

### **Medicare Supplement**

Annual statement disclosures on Medicare supplement business together with the review of various balance sheet items revealed several accounting and record keeping issues which include the following:

- Premium amounts in the annual statements for Medicare supplement were forced;
- Unpaid claims liabilities were not reported;
- Premium liabilities were not reported.

The Organization provided estimates of \$1,832,897 for premiums uncollected from the years 2000 and 2001 from its parent, \$200,000 for unrecorded unpaid claims and \$31,086 for unrecorded unearned and advanced premiums. No adjustments to balance sheet items were considered appropriate or necessary due to the minimal resulting effects on allowable assets and changes in capital and surplus.

## **FINANCIAL STATEMENTS**

The following financial statements were included in this report:

Balance Sheet as of December 31, 2001

Statement of Revenues and Expenses, Year Ending December 31, 2001

Capital and Surplus Account, Three Year Period Ending December 31, 2001

**The comments to financial statements are an integral  
part of the financial statements.**

**Healthwise**  
**Balance Sheet as of December 31, 2001**

**Assets**

Bonds	\$24,958,133	
Common stocks	6,117,125	
Cash and short term investments	3,683,528	
Receivable for securities	213,724	
Accident and health premiums due and unpaid	1,334,053	(1)*
Investment income due and accrued	354,682	
Amounts receivable relating to uninsured accident and health plans	689,861	(2)*
Federal and foreign income tax recoverable and interest thereon	<u>226,778</u>	
Total assets (per exam)	<u>\$37,577,884</u>	

**Liabilities, Capital and Surplus**

Claims unpaid	\$ 3,676,094	(3)*
Unpaid claims adjustment expenses	200,000	
Aggregate policy reserves	18,220	
Premiums received in advance	615,029	
General expenses due or accrued	274,633	
Federal and foreign income tax payable and interest thereon	1,042,871	
Amounts withheld or retained for the account of others	300,696	(4)*
Amounts due to parent, subsidiaries and affiliates	41,256	
Payable for securities	1,318,872	
Retrospective settlement	82,022	
Suspense deposit	<u>43,171</u>	
Total liabilities	<u>7,612,864</u>	
Common capital stock	233,360	(5)*
Gross paid in and contributed surplus	3,766,800	(6)*
Unassigned funds (surplus)	<u>25,964,860</u>	(7)*
Total capital and surplus	<u>29,965,020</u>	
Total liabilities, capital and surplus	<u>\$37,577,884</u>	

**\* Refer to Comments to Financial Statements**

**Healthwise  
Statement of Revenue and Expenses  
Year Ending December 31, 2001**

MEMBER MONTHS	<u>364,799</u>
Net premium income	\$32,292,094
Change in unearned premium reserves and reserve rate credits	<u>(11,045)</u>
Total revenues	<u>32,281,049</u>
Medical and Hospital	
Hospital/medical benefits	11,616,599
Other professional services	6,210,259
Emergency room and out-of-area	1,271,811
Other medical and hospital expenses	<u>3,930,895</u>
Subtotal	23,029,564
Claims adjustment expenses	1,426,988
General administrative expenses	<u>4,186,802</u>
Total underwriting deductions	<u>28,643,354</u>
Net underwriting gain or (loss)	<u>3,637,695</u>
Net investment income earned	1,492,748
Net realized capital gains or (losses)	<u>201,309</u>
Net investment gains or (losses)	1,694,057
Misc. income/expense	<u>(218,030)</u>
Net income or (loss) before federal income taxes	5,113,722
Federal and foreign income taxes incurred	<u>867,541</u>
Net income (loss)	<u>\$ 4,246,181</u>

**Healthwise  
Capital and Surplus Account  
Three Year Period Ending December 31, 2001**

	<u><b>1999</b></u>	<u><b>2000</b></u>	<u><b>2001</b></u>
Capital and surplus, December 31, prior year	<u>\$19,361,697</u>	<u>\$14,999,902</u>	<u>\$24,477,709</u>
Net income	2,551,798	2,913,671	4,246,181
Net unrealized capital gains and losses	145,327	(487,280)	(893,778)
Change in net deferred income taxes	0	0	363,715
Change in nonadmitted assets	(7,058,920)	7,051,416	1,576,754
Cumulative effect of changes in accounting principles	<u>0</u>	<u>0</u>	<u>194,439</u>
Net change in capital and surplus	<u>(4,361,795)</u>	<u>9,477,807</u>	<u>5,487,311</u>
Capital and surplus, December 31, current year	<u><b>\$14,999,902</b></u>	<u><b>\$24,477,709</b></u>	<u><b>\$29,965,020</b></u>

## **COMMENTS TO FINANCIAL STATEMENTS**

### **(1) Accident and health premiums due and unpaid** **\$1,334,053**

The asset was reduced by \$689,861 for self funded claims receivable. The amount was reclassified to the amounts receivable relating to the uninsured accident and health plans item in accordance with the NAIC's Annual Statement Instructions. The Organization had subsequently corrected the misclassification prior to this examination. The result had no effect on surplus.

### **(2) Amounts receivable relating to uninsured accident and health plans** **\$689,861**

The asset was increased by \$689,861 for self funded claims receivable which were included in the accident and health premiums due and unpaid item in error. Refer to Comment to Financial Statements #1. The result had no effect on surplus.

### **(3) Unpaid claims** **\$3,676,094**

The liability was increased by \$456,096, which is the amount of processed but unpaid claims net of overpayments to providers. Refer to Comment to Financial Statements #4.

### **(4) Amounts withheld or retained by company for the account of others** **\$300,696**

The liability was reduced by \$456,096 which was reclassified to unpaid claims. The amount of the reduction represented the net of a reduction to processed but unpaid claims (\$567,570) and an increase of a receivable for overpayments made to providers (\$111,476). The reclassification was done in order to comply with SSAP #55. These reclassifications had no resulting effect on surplus.

### **(5) Capital stock** **\$233,360**

The account was increased by \$233,360 to reclassify capital stock amounts from unassigned funds to be consistent with NAIC Annual Statement Instructions. Refer to Comment to Financial Statements #7.

### **(6) Gross paid in and contributed surplus** **\$3,766,800**

The account was increased by \$3,766,800 to reclassify gross paid in and contributed surplus amounts from unassigned funds to be consistent with NAIC Annual Statement Instructions. Refer to Comment to Financial Statements #7.

### **(7) Unassigned funds** **\$25,964,860**

This account was reduced by an aggregate amount of \$4,000,160 because all capital and surplus accounts were reported in the unassigned surplus account in noncompliance with the NAIC Annual Statement Instructions. Both the capital stock (\$233,360) and gross paid in and contributed surplus (\$3,766,800) amounts were reclassified to the appropriate accounts for examination purposes.



## CAPITAL AND SURPLUS

The Organization's minimum capital requirement was \$400,000 pursuant to UCA Subsection 31A-5-211(2)(a). Its total adjusted capital was \$29,965,020 and authorized control level risk based capital was \$1,480,412 pursuant to UCA Part 31A-17-VI.

The examination determined that gross paid in and contributed surplus was \$3,766,800 and unassigned funds were \$25,964,860. Adjustments to balance sheet items, as reflected below, had no resulting effect on capital and surplus.

<u>Account</u>	<u>Organization</u>	<u>Examination</u>	<u>Change in Surplus</u>
Accident and health premiums due and unpaid	\$ 2,023,914	\$ 1,334,053	\$ (689,861)
Amounts receivable relating to uninsured accident and health plans	0	689,861	689,861
Unpaid claims	3,220,000	3,676,094	(456,094)
Accounts withheld or retained for the account of others	756,790	300,696	456,094
Capital stock	0	233,360	233,360
Gross paid in and contributed surplus	0	3,766,800	3,766,800
Unassigned funds	29,965,020	25,964,860	(4,000,160)
Total examination changes			0
Capital and surplus - Organization			<u>29,965,020</u>
Capital and surplus - Examination			<u>\$29,965,020</u>

## SUMMARY

This report contained the following comments deemed to be of significance:

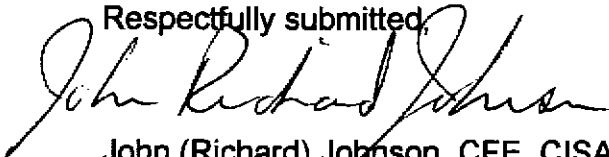
1. The only active committee of the board of directors had only two members, in noncompliance with UCA Subsection 31A-5-412(1). (Management)
2. No signed conflict of interest questionnaires were provided for the year 2001 for two of the directors, which was in non-compliance with Article VIII of the bylaws of the Organization. (Conflict of Interest)
3. Minutes of the board of directors meetings provided no evidence the copies of the prior report of examination were furnished to its members as required by UCA Subsection 31A-2-204(8). (Corporate Records)
4. The board of directors neglected to elect an assistant secretary or an assistant treasurer for the years 2000 and 2001, as required in the bylaws of the Organization. (Corporate Records)

5. The sale of a matured bond included in statutory deposits without the approval of the Insurance Commissioner was in noncompliance with UCA Subsection 31A-2-206(10). (Statutory Deposits)
6. The Organization had several instances of non-compliance with NAIC Annual Statement Instructions, as detailed in Accounts and Records and Comments to Financial Statements. In addition, the Organization's copy of a bank signatory card was not consistent with the copy of the signatory card provided by the bank. (Accounts and Records and Comments to Financial Statements)

### CONCLUSION

The courteous and prompt assistance and cooperation extended by officers and employees of the Organization during the course of this examination is acknowledged.

Respectfully submitted,



John (Richard) Johnson, CFE, CISA  
Senior Financial Examiner  
Utah Insurance Department